

Mortgage Loan Programs Subsidy Recapture Overview



Minnesota Housing has been helping homebuyers finance homes for more than 40 years, partnering with a statewide network of approved lenders to offer safe and affordable home loans.

The Reason for Recapture

The below-market rate on your Start Up loan or the benefit you receive through the Mortgage Credit Certificate (MCC) Program has been made possible through Minnesota Housing's use of tax-exempt bonding authority. The Internal Revenue Code enables the federal government to recoup some of the tax-exempt subsidy under certain conditions. The recapture is accomplished by an increase in your federal income tax for the year in which you sell your home.

For most homebuyers, the financial benefits of both homeownership (i.e., deductions for mortgage interest and taxes) and participating in a Minnesota Housing program (lower interest rate, federal income tax credit and/or downpayment assistance) far outweigh the possibility of subsidy recapture.

What Triggers Recapture?

To owe recapture tax, **all three** of the following criteria **must** apply. Homeowners must:

- Sell their home within the first nine years after closing the loan;
- Have a household income above a specified amount (see pages four and five of the Subsidy Recapture Disclosure Statement and Tennesen Warning form for income limits); **and**,
- Realize a gain from the sale of the home as defined by the IRS (this is different from exposure to capital gains tax)

If even one of the above criteria does not apply, subsidy recapture is not triggered.

While a refinance does not trigger payment of the tax, it also does not eliminate the recapture tax, which remains in place for the nine-year period from the original loan closing.

What if My Home is in a Targeted Area?

Targeted Areas consist of certain census tracts in the state in which 70% of the families have an annual income of 80% or less of the statewide median income. Very few census tracts meet this definition. However, if you buy a home in a Targeted Area, a higher total household income threshold applies to borrowers in order to trigger subsidy recapture. The total household income thresholds for Targeted Areas are listed on page five of the Subsidy Recapture Disclosure Statement and Tennesen Warning form.

What If Recapture Tax Has To Be Paid?

Most homebuyers will **never** have to pay any recapture tax. For the few who do meet **all three** conditions, they must pay the recapture tax to the IRS when they file their federal income tax return for the year in which the home is sold. The recapture amount will be determined separately according to the respective interests in the residence when two or more persons (generally unmarried) receive a Start-Up Loan or an MCC.

The homeowner is responsible for the calculation and payment to the federal government. The originating lender is only responsible for disclosure at time of application and closing.

Even if the recapture tax must be paid, the tax provisions are structured to limit the amount homeowners pay. Borrowers will never pay more 6.25% of the original principal amount of their first mortgage loan. In addition, the overall repayment may be reduced by the following factors:

- Holding period percentage – The percentage of the recapture tax adjusts depending on how long the borrower has been in the home.
- Income percentage – If the borrower's income exceeds the maximum income limit, but not by more than \$5,000, only a percentage of the tax must be paid.
- The repayment tax cannot exceed 50% of the gain on sale.

Questions about Recapture

For questions about paying the tax, homeowners should consult a tax specialist or the IRS at 1-800-829-1040.